

AMENDED IN ASSEMBLY JANUARY 13, 2000

AMENDED IN ASSEMBLY JANUARY 3, 2000

CALIFORNIA LEGISLATURE—1999–2000 REGULAR SESSION

ASSEMBLY BILL

No. 488

Introduced by Assembly Member Ducheny
(Coauthors: Assembly Members Alquist and Honda)

February 18, 1999

An act to amend Section 23609 of, and to add Sections 23609.1 and 23609.2 to and repeal Section 23609.1 of, the Revenue and Taxation Code, relating to taxation, to take effect immediately, tax levy.

LEGISLATIVE COUNSEL'S DIGEST

AB 488, as amended, Ducheny. Bank and corporation tax law: credits: ~~deductions~~.

The Bank and Corporation Tax Law allows various credits and ~~deductions~~ in computing taxes, including a credit for, and a ~~net operating loss deduction~~ for, certain expenses for research and development.

This bill would, in the case of biotechnology and technology companies, provide that a portion of those credits and ~~net operating loss deductions~~ may be transferred to other corporations or ~~surrendered to the state for a refund~~, as provided.

This bill would take effect immediately as a tax levy.

Vote: majority. Appropriation: no. Fiscal committee: yes. State-mandated local program: no.

The people of the State of California do enact as follows:

1 SECTION 1. Section 23609 of the Revenue and
2 Taxation Code is amended to read:
3 23609. For each income year beginning on or after
4 January 1, 1987, there shall be allowed as a credit against
5 the “tax” (as defined by Section 23036) an amount
6 determined in accordance with Section 41 of the Internal
7 Revenue Code, except as follows:
8 (a) For each income year beginning before January 1,
9 1997, both of the following modifications shall apply:
10 (1) The reference to “20 percent” in Section 41(a)(1)
11 of the Internal Revenue Code is modified to read “8
12 percent.”
13 (2) The reference to “20 percent” in Section 41(a)(2)
14 of the Internal Revenue Code is modified to read “12
15 percent.”
16 (b) (1) For each income year beginning on or after
17 January 1, 1997, and before January 1, 1999, both of the
18 following modifications shall apply:
19 (A) The reference to “20 percent” in Section 41(a)(1)
20 of the Internal Revenue Code is modified to read “11
21 percent.”
22 (B) The reference to “20 percent” in Section 41(a)(2)
23 of the Internal Revenue Code is modified to read “24
24 percent.”
25 (2) For each income year beginning on or after
26 January 1, 1999, both of the following shall apply:
27 (A) The reference to “20 percent” in Section 41(a)(1)
28 of the Internal Revenue Code is modified to read “12
29 percent.”
30 (B) The reference to “20 percent” in Section 41(a)(2)
31 of the Internal Revenue Code is modified to read “24
32 percent.”
33 (c) (1) With respect to any expense paid or incurred
34 after the operative date of Section 6378, Section 41(b)(1)
35 of the Internal Revenue Code is modified to exclude from
36 the definition of “qualified research expense” any
37 amount paid or incurred for tangible personal property

1 that is eligible for the exemption from sales or use tax
2 provided by Section 6378.

3 (2) “Qualified research” and “basic research” shall
4 include only research conducted in California.

5 (d) The provisions of Section 41(e)(7)(A) of the
6 Internal Revenue Code, shall be modified so that “basic
7 research,” for purposes of this section, includes any basic
8 or applied research including scientific inquiry or original
9 investigation for the advancement of scientific or
10 engineering knowledge or the improved effectiveness of
11 commercial products, except that the term does not
12 include any of the following:

13 (1) Basic research conducted outside California.

14 (2) Basic research in the social sciences, arts, or
15 humanities.

16 (3) Basic research for the purpose of improving a
17 commercial product if the improvements relate to style,
18 taste, cosmetic, or seasonal design factors.

19 (4) Any expenditure paid or incurred for the purpose
20 of ascertaining the existence, location, extent, or quality
21 of any deposit of ore or other mineral (including oil and
22 gas).

23 (e) (1) In the case of a taxpayer engaged in any
24 biopharmaceutical research activities that are described
25 in codes 2833 to 2836, inclusive, or any research activities
26 that are described in codes 3826, 3829, or 3841 to 3845,
27 inclusive, of the Standard Industrial Classification (SIC)
28 Manual published by the United States Office of
29 Management and Budget, 1987 edition, or any other
30 biotechnology research and development activities, the
31 provisions of Section 41(e)(6) of the Internal Revenue
32 Code shall be modified to include both of the following:

33 (A) A qualified organization as described in Section
34 170(b)(1)(A)(iii) of the Internal Revenue Code and
35 owned by an institution of higher education as described
36 in Section 3304(f) of the Internal Revenue Code.

37 (B) A charitable research hospital owned by an
38 organization that is described in Section 501(c)(3) of the
39 Internal Revenue Code, is exempt from taxation under
40 Section 501(a) of the Internal Revenue Code, is not a

1 private foundation, is designated a “specialized
2 laboratory cancer center,” and has received Clinical
3 Cancer Research Center status from the National Cancer
4 Institute.

5 (2) For purposes of this subdivision:

6 (A) “Biopharmaceutical research activities” means
7 those activities that use organisms or materials derived
8 from organisms, and their cellular, subcellular, or
9 molecular components, in order to provide
10 pharmaceutical products for human or animal
11 therapeutics and diagnostics. Biopharmaceutical
12 activities make use of living organisms to make
13 commercial products, as opposed to pharmaceutical
14 activities that make use of chemical compounds to
15 produce commercial products.

16 (B) “Other biotechnology research and development
17 activities” means research and development activities
18 consisting of the application of recombinant DNA
19 technology to produce commercial products, as well as
20 research and development activities regarding
21 pharmaceutical delivery systems designed to provide a
22 measure of control over the rate, duration, and site of
23 pharmaceutical delivery.

24 (f) In the case where the credit allowed by this section
25 exceeds the “tax,” the excess may be carried over to
26 reduce the “tax” in the following year, and succeeding
27 years if necessary, until the credit has been exhausted.

28 (g) For each income year beginning on or after
29 January 1, 1998, the reference to “Section 501(a)” in
30 Section 41(b)(3)(C) of the Internal Revenue Code,
31 relating to contract research expenses, is modified to read
32 “this part or Part 10 (commencing with Section 17001).”

33 (h) (1) For each income year beginning on or after
34 January 1, 1998:

35 (A) The reference to “1.65 percent” in Section
36 41(c)(4)(A)(i) of the Internal Revenue Code is modified
37 to read “one and thirty-two hundredths of one percent.”

38 (B) The reference to “2.2 percent” in Section
39 41(c)(4)(A)(ii) of the Internal Revenue Code is

1 modified to read “one and seventy-six hundredths of one
2 percent.”

3 (C) The reference to “2.75 percent” in Section
4 41(c)(4)(A)(iii) of the Internal Revenue Code is
5 modified to read “two and two-tenths of one percent.”

6 (2) Section 41(c)(4)(B) shall not apply and in lieu
7 thereof an election under Section 41(c)(4)(A) of the
8 Internal Revenue Code may be made for any income year
9 of the taxpayer beginning on or after January 1, 1998. That
10 election shall apply to the income year for which made
11 and all succeeding income years unless revoked with the
12 consent of the Franchise Tax Board.

13 (3) Section 41(c)(6) of the Internal Revenue Code,
14 relating to gross receipts, is modified to take into account
15 only those gross receipts from the sale of property held
16 primarily for sale to customers in the ordinary course of
17 the taxpayer’s trade or business that is delivered or
18 shipped to a purchaser within this state, regardless of
19 f.o.b. point or any other condition of the sale.

20 (i) Section 41(h) of the Internal Revenue Code,
21 relating to termination, shall not apply.

22 (j) Section 41(g) of the Internal Revenue Code,
23 relating to special rule for passthrough of credit, is
24 modified by each of the following:

25 (1) The last sentence shall not apply.

26 (2) If the amount determined under Section 41(a) of
27 the Internal Revenue Code for any income year exceeds
28 the limitation of Section 41(g) of the Internal Revenue
29 Code, that amount may be carried over to other income
30 years under the rules of subdivision (f), except that the
31 limitation of Section 41(g) of the Internal Revenue Code
32 shall be taken into account in each subsequent income
33 year.

34 (k) ~~In~~ *For income years beginning on or after January*
35 *1, 2000, and before January 1, 2006, in the case of a*
36 *taxpayer that is a biotechnology or technology company,*
37 *as defined by Section 23609.1, and is a partner in a*
38 *partnership with a biotechnology or technology*
39 *company, the taxpayer’s share of qualified research*
40 *expenses or basic research payments, or share of the*

1 credit computed under Section 41(a) of the Internal
2 Revenue Code by the partnership, shall equal the sum of
3 both of the following:

4 (1) The taxpayer's share of qualified research expenses
5 and basic research payments, or share of the credit
6 computed under Section 41(a) of the Internal Revenue
7 Code by the partnership, allocated or apportioned to that
8 partner under Section 704 of the Internal Revenue Code.

9 (2) If any other partner in the partnership agrees, all
10 or a portion of the share of the item that is allocated or
11 apportioned to the other partner under Section 704 of the
12 Internal Revenue Code.

13 The total qualified research expenses and basic
14 research payments, or total credit under Section 41(a) of
15 the Internal Revenue Code, for the income year with
16 respect to any partner may not exceed 125 percent of the
17 amount that would be allocated or apportioned under
18 paragraph (1). Any partner that agrees to permit another
19 partner to treat all or a portion of the first partner's
20 allocated or apportioned share of qualified research
21 expenses and basic research payments, or share of the
22 credit under Section 41(a) of the Internal Revenue Code
23 computed by the partnership, under paragraph (2)
24 above shall reduce its share of that item by the amount
25 allocated or apportioned to the other partner under
26 paragraph (2).

27 SEC. 2. Section 23609.1 is added to the Revenue and
28 Taxation Code, to read:

29 23609.1. (a) For purposes of this section:

30 (1) "Biotechnology company" means a corporation
31 that *is primarily engaged in research and development*
32 *activities that are described in Code 541710 of the North*
33 *American Industry Classification System Manual*
34 *published by the United States Office of Management*
35 *and Budget, 1997 edition, and that* has its headquarters or
36 base of operations in this state and that is engaged in
37 research and development activities regarding:
38 organisms or materials derived from organisms, and their
39 cellular, subcellular, or molecular components, in order
40 to provide pharmaceutical products; recombinant DNA

1 technology to produce commercial products; or
2 pharmaceutical delivery systems designed to provide a
3 measure of control over the rate, duration, and site of
4 pharmaceutical delivery.

5 (2) “Technology company” means a corporation that
6 *is primarily engaged in computer and electronic product*
7 *manufacturing as described in Sector 334 of the North*
8 *American Industry Classification System Manual*
9 *published by the United States office of Management and*
10 *Budget, 1997 edition, and that* has its headquarters or base
11 of operations in this state and that employs highly
12 educated or highly trained managers and workers who
13 use sophisticated scientific research service or production
14 equipment, process, or knowledge to discover, develop,
15 test, transfer, or manufacture a product or service.

16 (3) “Unused tax benefits” means unused amounts of
17 tax credits for increased research activities permitted to
18 be carried over pursuant to subdivision (d) of Section
19 ~~23609 or unused net operating loss deductions permitted~~
20 ~~to be carried over pursuant to subdivision (b) of Section~~
21 ~~24416. 23609.~~

22 (b) (1) Any biotechnology or technology company
23 with unused tax benefits shall be allowed to transfer those
24 tax benefits for use by other corporation business
25 taxpayers in the State of California provided that (A) the
26 taxpayer receiving the transferred tax benefits *is a*
27 *biotechnology or technology company, and* is not
28 affiliated with the corporation that is transferring its tax
29 benefits pursuant to this paragraph, and (B) that
30 transferee taxpayer pays to the transferor taxpayer an
31 amount equal to at least 75 percent of the value of the
32 transferred tax benefit.

33 (2) For purposes of this section, the test for affiliation
34 is whether the same entity directly or indirectly owns or
35 controls 10 percent or more of the voting rights or 10
36 percent of the value of all classes of stock of both the
37 taxpayer receiving the benefits and the corporation that
38 is transferring the benefits.

39 (3) The value of the transferred tax benefit for a
40 research and development tax credit carryover is the

~~1 amount of the credit. The value of the transferred tax~~
~~2 benefit for a net operating loss carryover is the amount of~~
~~3 the loss (A) multiplied by the biotechnology or~~
~~4 technology company's applicable allocation factor, as~~
~~5 determined in accordance with Sections 25120 to 25139,~~
~~6 inclusive, for the year in which the benefit is transferred,~~
~~7 (B) divided by the transferee taxpayer's applicable~~
~~8 allocation factor for that year, and (C) multiplied by the~~
~~9 corporate tax rate set forth in Section 23151. The amount~~
10 *of the credit. The* maximum lifetime value of transferred
11 tax benefits that a corporation shall be permitted to
12 transfer pursuant to this section is twenty million dollars
13 (\$20,000,000).

14 (4) The private financial assistance shall be used to
15 fund expenses incurred in connection with the operation
16 of a biotechnology company or technology company in
17 this state, including, but not limited to, expenses of fixed
18 assets, such as construction and acquisition and
19 development of real estate, materials, startup, tenant
20 fit-out, working capital, salaries, and research and
21 development expenditures.

22 (5) To the extent unused tax benefits have been
23 transferred pursuant to this section, a transferor taxpayer
24 is prohibited from claiming the tax benefits on its tax
25 return or transferring the tax benefits more than one
26 time.

27 (6) The Franchise Tax Board shall maintain a
28 cumulative total of the value of all unused tax benefits
29 transferred by taxpayers pursuant to this section in a
30 particular income year. At least 30 days prior to the
31 transfer of unused tax benefits pursuant to this section,
32 the proposed transferor taxpayer shall notify the
33 Franchise Tax Board of the value of the unused tax
34 benefit being transferred. With respect to each proposed
35 transfer of unused tax benefits, the cumulative total value
36 of transferred tax benefits shall be computed as of the
37 time the Franchise Tax Board is notified of the proposed
38 transfer of unused tax benefits. If the cumulative total
39 value of the transferred tax benefits exceeds the
40 maximum annual transferred tax benefits, the Franchise

1 Tax Board shall promptly notify the proposed transferor
2 taxpayer that the transfer is authorized by this section
3 only to the extent that the tax benefits do not exceed the
4 maximum annual transferred tax benefits. For purposes
5 of this section, the maximum annual transferred tax
6 benefits shall be twenty-five million dollars (\$25,000,000).

7 ~~SEC. 3. Section 23609.2 is added to the Revenue and~~
8 ~~Taxation Code, to read:~~

9 ~~23609.2. (a) For purposes of this section:~~

10 ~~(1) "Biotechnology company" means a corporation~~
11 ~~that has its headquarters or base of operations in this state~~
12 ~~and that is engaged in research and development~~
13 ~~activities regarding organisms or materials derived from~~
14 ~~organisms, and their cellular, subcellular, or molecular~~
15 ~~components, in order to provide pharmaceutical~~
16 ~~products; or recombinant DNA technology to produce~~
17 ~~commercial products, or pharmaceutical delivery~~
18 ~~systems designed to provide a measure of control over the~~
19 ~~rate, duration, and site of pharmaceutical delivery.~~

20 ~~(2) "Technology company" means a corporation that~~
21 ~~has its headquarters or base of operations in this state and~~
22 ~~that employs highly educated or highly trained managers~~
23 ~~and workers who use sophisticated scientific research~~
24 ~~service or production equipment, process, or knowledge~~
25 ~~to discover, develop, test, transfer, or manufacture a~~
26 ~~product or service.~~

27 ~~(3) "Unused tax benefits" means unused amounts of~~
28 ~~tax credits for increased research activities permitted to~~
29 ~~be carried over pursuant to subdivision (d) of Section~~
30 ~~23609 or unused net operating loss deductions permitted~~
31 ~~to be carried over pursuant to subdivision (b) of Section~~
32 ~~24416.~~

33 ~~(b) (1) Any biotechnology or technology company~~
34 ~~with unused tax benefits shall receive a refund, without~~
35 ~~regard to the amount of any tax previously paid, equal to~~
36 ~~50 percent of the value of the unused tax benefits that are~~
37 ~~surrendered to this state. Unused tax benefits shall be~~
38 ~~surrendered and a refund for the surrendered unused tax~~
39 ~~benefits shall be claimed by showing those amounts and~~

1 ~~claiming the refund on an original or amended income~~
2 ~~tax return.~~

3 ~~(2) The value of the surrendered tax benefit for a~~
4 ~~research and development tax credit carryover is the~~
5 ~~amount of the credit. The value of the surrendered tax~~
6 ~~benefit for a net operating loss carryover is the amount of~~
7 ~~the loss (A) multiplied by the biotechnology or~~
8 ~~technology company's applicable allocation factor, as~~
9 ~~determined in accordance with Sections 25120 to 25139,~~
10 ~~inclusive, for the year in which the benefit is surrendered;~~
11 ~~and (B) multiplied by the corporate tax rate set forth in~~
12 ~~Section 23151 for that year. The maximum lifetime refund~~
13 ~~that may be received by a corporation and its affiliated~~
14 ~~corporation business taxpayers pursuant to this section is~~
15 ~~twenty million dollars (\$20,000,000).~~

16 ~~(3) For purposes of this section, a corporation is~~
17 ~~affiliated with the taxpayer if either the taxpayer directly~~
18 ~~or indirectly owns or controls 10 percent or more of the~~
19 ~~voting rights or 10 percent of the value of all classes of~~
20 ~~stock of that corporation or another organization directly~~
21 ~~or indirectly owns or controls 10 percent or more of the~~
22 ~~voting rights or 10 percent of the value of all classes of~~
23 ~~stock of both taxpayer and that corporation.~~

24 ~~(4) To the extent unused tax benefits have been~~
25 ~~surrendered pursuant to this section, a surrendering~~
26 ~~taxpayer is prohibited from claiming the tax benefits on~~
27 ~~its tax return or surrendering the tax benefits more than~~
28 ~~one time.~~

29 ~~(5) The Franchise Tax Board shall maintain a~~
30 ~~cumulative total of the value of all unused tax benefits~~
31 ~~surrendered by taxpayers pursuant to this section in a~~
32 ~~particular income year. At least 30 days prior to the~~
33 ~~surrender of unused tax benefits pursuant to this section,~~
34 ~~the surrendering taxpayer shall notify the Franchise Tax~~
35 ~~Board of the value of the unused tax benefit being~~
36 ~~surrendered. With respect to each proposed surrender of~~
37 ~~unused tax benefits, the cumulative total value of~~
38 ~~surrendered tax benefits shall be computed as of the time~~
39 ~~the Franchise Tax Board is notified of the proposed~~
40 ~~surrender of unused tax benefits. If the cumulative total~~

~~value of the surrendered tax benefits exceeds the maximum annual surrendered tax benefits, the Franchise Tax Board shall promptly notify the surrendering taxpayer that the surrender is authorized by this section only to the extent that the tax benefits do not exceed the maximum annual surrendered tax benefits. For purposes of this section, the maximum annual surrendered tax benefits shall be twenty-five million dollars (\$25,000,000).~~

~~SEC. 4. This act provides for a tax levy within the meaning of Article IV of the Constitution and shall go into immediate effect.~~

~~(c) This section shall remain in effect only until December 1, 2006, and as of that date is repealed.~~

~~SEC. 3. The Franchise Tax Board shall report to the Legislature by January 1, 2005, on the number and costs of the tax credits transferred pursuant to this act.~~

~~SEC. 4. This act provides for a tax levy within the meaning of Article IV of the Constitution and shall go into immediate effect.~~